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No. 93-516

In The

Supreme Court of the United States

October Term, 1993

HEARTLAND FEDERAL SAVINGS AND LOAN ASSOCIATION,

Petitioner,

vs.

BRISCOE ENTERPRISES, LTD., II,

Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

RESPONDENT'S BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

This case involves a chapter 11 plan of reorganization that was confirmed under the "cramdown" provisions of 11 U.S.C. § 1129(b), and which confirmation was affirmed by the Fifth Circuit Court of Appeals.

1. Should this Court grant a writ of certiorari where the Fifth Circuit Court of Appeals has applied the *preponderance of the evidence* standard to 11 U.S.C. § 1129(b) consistent with decisions of this Court, and where the Court of Appeals Opinion below is the only circuit court decision to determine this issue.

2. Should this Court grant a writ of certiorari where the Fifth Circuit Court of Appeals, after reviewing the record evidence heard by the bankruptcy court, found that the proponent of the plan of reorganization met its burden of proof under the "fair and equitable" standard of 11 U.S.C. § 1129(b).

3. Should this Court grant a writ of certiorari to determine whether to adopt a *per se* rule requiring different treatment of similar but separately classified claims when no circuit court has adopted a *per se* rule.

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RESPONDENT'S BRIEF IN OPPOSITION

TO THE UNITED STATES SUPREME COURT:

Briscoe Enterprises, Ltd., II ("Briscoe") files this Brief in Opposition to Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit ("Response"), asking this Court to deny the petition for writ of certiorari ("Petition") to review the opinion issued July 13, 1993 by the United States Court of Appeals for the Fifth Circuit. In support of this request, Briscoe would respectfully show the Court as follows:

JURISDICTION

In addition to the jurisdictional facts listed by Heartland, Briscoe notes that the bankruptcy court had jurisdiction to confirm Briscoe's plan of reorganization pursuant to both 28 U.S.C. § 1334 and § 157. With respect to the appellate court decision at issue, the Fifth Circuit denied both Heartland's Motion for Rehearing and its Suggestion for Rehearing *En Banc* on August 16, 1993. *Briscoe Enters., Ltd., II v. Heartland Fed. Sav. & Loan Ass'n (In re Briscoe)*, 994 F.2d 1160 (5th Cir. 1993); Pet. App. at 1-26 (the "Court of Appeals Opinion").

STATEMENT OF THE CASE

Briscoe owns and operates Regalridge Square Apartments ("Regalridge" or the "Property"), a 784-unit apartment complex located in southeast Fort Worth, Texas. Regalridge serves low- to moderate-income families, many of whom receive rental subsidies from the federal government. In addition, the City of Fort Worth (the "City"), through its Rental Assistance Program, contributes approximately $20,000 a month for rental subsidies on behalf of Regalridge residents.

Briscoe's Plan of Reorganization (the "Plan") provides generally for continued operation of Regalridge as a quality residential community for a largely African-American population and for payment of creditor claims. On the effective date of the Plan, the Regalridge property will be transferred to the Regalridge Trust for the benefit of creditors. The Regalridge Trust will be managed by a panel of three trustees, one each appointed by Heartland,

the City, and the Fort Worth NAACP. All equity interests in Briscoe will be cancelled, and interest holders will receive nothing under the Plan. The Plan also provides for creation of a Distribution Fund (as defined in the Plan), by which the City may provide approximately $150,000 for additional tenant subsidies in the future.

In its Petition, Heartland misstates several facts concerning the classification scheme and voting, although Briscoe would point out that these do not affect the gravamen of Heartland's complaint, *i.e.*, that the City's unsecured claim was treated the same, but classified separately from the other unsecured claims.

Heartland misstates that its unsecured claim was placed with that of other unsecured claims in Class 5 and that Class 5 voted against the Plan. Pet. at 6, 17. The facts as stated in the Court of Appeals Opinion are correct. Heartland's entire claim (both the secured and unsecured portion) was placed in Class 4 (which voted against the Plan), but the unsecured portion of Heartland's claim would be treated like that of the unsecured claims in Class 5. 994 F.2d at 1163; Pet. App. at 4-5. Class 5 (other unsecured claims), as well as Class 3 (the City's unsecured claim) and Class 2 (the City's secured ad valorem tax claim) voted for the Plan.

The bankruptcy court conducted five days of hearings that included testimony from eight witnesses. The bankruptcy judge conducted a personal inspection of the property with counsel present. 994 F.2d at 1162; Pet. App. at 3. Based on this evidence, the bankruptcy court found that Respondent Briscoe had met its burden of proof and confirmed the Plan. The district court reversed, but the

Fifth Circuit Court of Appeals, in a unanimous nine-page opinion authored by Judge Wisdom, reversed the district court and affirmed the confirmation order of the bankruptcy court.

SUMMARY OF THE ARGUMENT

The Fifth Circuit's application of the preponderance of the evidence standard to the cramdown provisions of the Bankruptcy Code does not warrant review by this Court because the decision correctly applies this Court's precedent and there is no circuit conflict. The opinion of the Court of Appeals is the only circuit court decision that determines what standard of proof applies to cramdown.

The Fifth Circuit did not shift the burden of proving the reorganization plan was fair and equitable from Briscoe, the plan proponent, to Heartland. In a supplemental letter brief to the Fifth Circuit, Briscoe summarized and cited relevant evidence it had presented in four days of hearings. In reaching its conclusion that the Plan was fair and equitable to Heartland, the Court of Appeals Opinion adverts to "the evidence presented to the bankruptcy court" and discusses specific relevant facts, *e.g.*, whether the interest rate would adequately compensate Heartland and that Heartland had the right to foreclose under the plan.

Heartland requests this Court to engraft a *per se* rule that, to justify classifying similar claims separately, the plan proponent must treat the classes differently. The issue is not worthy of review for a number of reasons.

There is no conflict between the circuits: each one to address this issue has recognized that good reasons may exist to justify separate classification. None of the circuits, however, has adopted a *per se* rule that such claims must receive different treatment (a purported indicator that "good reasons" exist to classify similar claims separately). Moreover, the proposed rule is misguided and does not prevent the mischief to be avoided – that of improper classification for the purpose of obtaining an affirmative class vote to enable the proponent to use the cramdown provisions. There is no need for this Court to intervene, because the circuit courts are harmoniously developing, on a case-by-case basis, the contours of the "good reasons" test to justify classifying similar claims separately. Finally, unique facts make this case an inappropriate candidate for certiorari to consider separate classification law because the creditor classified separately was the City of Fort Worth, which has non-creditor interests related to urban housing and which contributes $20,000 per month in rental assistance.

ARGUMENT

I. THE STANDARD OF PROOF ISSUE DOES NOT WARRANT REVIEW BY THIS COURT

The Fifth Circuit's application of the preponderance of the evidence standard to the cramdown provisions of the Bankruptcy Code does not warrant review by this Court. The decision does not conflict with any other circuit court opinion. Furthermore, the Court of Appeals

correctly applied this Court's holdings in *Grogan v. Garner*, 498 U.S. 279 (1991) and *Addington v. Texas*, 441 U.S. 418 (1979). Moreover, the decision here is in full accord with the only circuit-level decision applying *Grogan*.

A. THERE IS NO CONFLICT BETWEEN THE FIFTH CIRCUIT'S DECISION AND DECISIONS OF OTHER CIRCUIT COURTS

In an effort to create the appearance of conflict with other circuits, Heartland cites a string of seven decisions for the proposition that clear and convincing proof is required in a cramdown. None of these is a circuit court decision. Further, none of the seven decisions includes a reasoned discussion or any explanation of why the appropriate evidentiary standard should be more than a preponderance. Indeed, the Court of Appeals Opinion is the *only* decision that applies *Grogan* in analyzing what standard of proof applies to section 1129 of the Bankruptcy Code.[1]

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[1] Heartland asserts that there is a "risk of confusion" because of decisions applying the clear and convincing standard in the context of particular contested matters in a bankruptcy case. This assertion is without merit because the cases cited by Heartland were either decided before *Grogan* or do not involve the application of a provision of the Bankruptcy Code. For example, *In re Vermont Toy Works, Inc.*, 135 B.R. 762 (D. Vt. 1991) involved the application of *state law* – the common law of marshalling – in a bankruptcy case.

B. APPLYING THE PREPONDERANCE STANDARD TO CRAMDOWN IS THE LOGICAL EXTENSION OF THE *GROGAN* DECISION

In *Grogan*, this Court held that the preponderance standard is applicable in actions to determine whether particular debts are dischargeable under 11 U.S.C. section 523. In reaching this conclusion, the Court noted that the statute and legislative history were silent concerning the standard of proof and further stated that

> [T]his silence is inconsistent with the view that Congress intended to require a special, heightened standard of proof. Because the preponderance of the evidence standard results in a roughly equal allocation of the risk of error between litigants, we presume that this standard is applicable in civil actions between private litigants unless "particularly important individual interests or rights are at stake."

Grogan, 498 U.S. at 286 (citing *Herman & MacLean v. Huddleston*, 459 U.S. 375 (1983) and *Addington v. Texas*, 441 U.S. 418 (1979)). Even though the clear and convincing standard had historically been applied in fraud cases, this Court found no "important individual interests" at stake and held that preponderance of the evidence is the appropriate standard under section 523 of the Bankruptcy Code. *Id.*

Following the reasoning process in *Grogan*, the Court of Appeals noted that the language of section 1129 and the legislative history were silent on the applicable burden of proof. After discussing *Herman & MacLean* and *Addington*, the Court of Appeals found no interests at stake that would trigger a heightened standard of proof,

concluding that this case is "solely about money."[2] 994 F.2d at 1164-65; Pet. App. at 8-11. As in *Grogan*, the Court of Appeals concluded that a heightened standard of proof above that of a preponderance of the evidence was not warranted.[3]

C. RATHER THAN CONFLICT WITH OTHER CIRCUITS, THE FIFTH CIRCUIT AND TENTH CIRCUIT HAVE FOLLOWED *GROGAN* TO THE SAME EFFECT

Far from creating a conflict, the Court of Appeals Opinion is fully in accord with existing law in other circuits. In *First National Bank v. Serafini*, 938 F.2d 1156 (10th Cir. 1991), the Tenth Circuit held that the preponderance standard, not the clear and convincing standard, is the appropriate standard in a dischargeability action brought pursuant to 11 U.S.C. section 727. *Id.* at 1157. Even though *Serafini* involved the discharge of a debtor under section 727, and not the dischargeability of a debt under section 523 as in *Grogan*, the Tenth Circuit stated that "we perceive no good reason to apply a different standard where § 727(a)(2) is involved." *Id.* Thus, the circuit courts that have applied *Grogan* are in complete

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[2] This language adverts to Chief Justice Burger's language in *Addington*, where he noted that the clear and convincing standard had been employed in civil cases when "the interests at stake are deemed to be more substantial than mere loss of money." 994 F.2d at 1164; Pet. App. at 8.

[3] If this Court wishes to signal that the Fifth Circuit properly applied *Grogan*, it could efficiently do so through a summary affirmance of the Court of Appeals Opinion under Rule 16.1 of the Rules of the Supreme Court.

agreement: if the statutory language and legislative history are silent as to the appropriate standard of proof and the interests at stake are not important individual interests, the ordinary preponderance standard applies.

II. THE FIFTH CIRCUIT DID NOT SHIFT THE BURDEN OF PROOF ON WHETHER A PLAN IS "FAIR AND EQUITABLE" ONTO THE PLAN OPPONENT

The Fifth Circuit did not shift from Briscoe to Heartland the burden of proving whether a plan is fair and equitable. The issue that Heartland raises is, in essence, a sufficiency of the evidence issue that is wholly unworthy of review by this Court.

The Court of Appeals Opinion shows that the court below relied on pertinent record evidence in concluding that Briscoe had met the cramdown requirements. 994 F.2d at 1169; Pet. App. at 20-23. The Court of Appeals explicitly adverted to the "evidence presented to the bankruptcy court" in its discussion preceding its conclusion that "the plan satisfies 1129(b)(2)(A)(i) [the "fair and equitable" requirement]." *Id.* Briscoe produced the relevant facts during a five-day hearing. Pertinent record evidence was explicitly detailed to the appellate court. *See* Resp. App. at 3-5.[4]

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[4] Supplemental to the briefing below, the appellate court invited the parties to respond to the views of Professor Warren. Briscoe's response was in a letter from Marilyn D. Garner to Susan Vaughn, which is reprinted in the Respondent's Appendix (hereinafter "Resp. App."). A portion of that response summarizes numerous record facts about Regalridge.

The essence of Heartland's argument is not that the court shifted the burden of proof, but that Briscoe's evidence was insufficient to establish fair and equitable treatment of Heartland. Indeed, Heartland admits in its Petition that "The [appellate] court determined that Briscoe had proved all the elements of the case" under the preponderance of the evidence standard. Pet. at 7. Heartland's argument below (and its real complaint here) was that the lower courts refused to *require* Briscoe to produce affirmative evidence of the value of the property in fifteen years. In fact, the appellate court specifically cautioned that any evidence of value in fifteen years was "inherently speculative." *Id.* The court, instead, sensibly focused upon immediate facts relevant to the issue of fairness, *i.e.*, that the interest rate was generous and that Heartland could foreclose if the reorganized debtor failed to service its debt.[5]

The passage from the Court of Appeals Opinion that troubles Heartland warrants quotation in full:

> Heartland and the district court suggest that allowing a balloon payment is unacceptable as there is no immediate indication from where the funds will come to pay off the balloon. As a

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[5] After carefully considering the record on appeal, the Court of Appeals concluded that 1) the Plan ensured that Heartland would have the right to foreclose if Briscoe failed to pay its debt service obligations, and 2) that the bankruptcy court's finding that a 10.25% interest rate adequately compensated Heartland for its risk was not clearly erroneous. The Court of Appeals then specifically acknowledged that the balloon payment added "some measure of risk," but concluded that "the interest rate appears adequate to cover this risk." 994 F.2d at 1168; Pet. App. at 22.

> general matter, many courts have held balloon payments to satisfy 1129(b).[6] It is reasonable to assume that the property itself will provide the source for the balloon payment.[7] There is no evidence that the property will decline in value. Therefore, when the balloon is due, either the property will be sold which will provide the balloon or refinancing will be possible. *Estimating property values fifteen years hence is inherently speculative, but the evidence presented to the bankruptcy court did not suggest that the property would decline in value so that the debtor would be unable to pay Heartland its remaining principal.* Therefore, we hold that the plan satisfies 1129(b)(2)(A)(i).

994 F.2d at 1169; Pet. App. at 22-23 (emphasis supplied).

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[6] In support, the Court of Appeals cites, in footnote 51, *In re Bryson Properties, XVIII*, 961 F.2d 496, 501 (4th Cir.), *cert. denied*, 113 S. Ct. 191 (1992) and *In re Guildford Telecasters, Inc.*, 128 B.R. 622, 627 (Bankr. M.D.N.C. 1991).

[7] Heartland would also imply that the appellate court based its decision upon an insupportable assumption, seizing upon the language that the court "assumed" that the property would provide the source for the balloon payment. Read in context, it is clear that this comment is in response to an argument raised by Heartland below. Heartland had argued that allowing a balloon payment was unacceptable as there was no immediate indication where the funds would come from to pay off the balloon. In the context of this single asset real estate case, where Heartland retains its senior lien, the appellate court gave this argument short shrift, stating "It is reasonable to assume that the property itself will provide the source for the balloon payment."

The emphasized passage makes clear that the court reviewed the *evidence presented to the bankruptcy court*.[8] That included, for example, Briscoe's evidence concerning the minimum income required to fund the Plan, historic income levels and occupancy levels in the apartment complex, and data concerning budget items, taxes and repairs. Resp. App. at 3-5.

Thus, the appellate court did not shift the burden of proof. Heartland has shown no grounds of error in the appellate court's careful examination of this fact-bound determination, let alone grounds that warrant review by this Court. While Heartland may take issue with the Fifth Circuit's determination that the Plan was "fair and equitable," it cannot maintain that the burden of proof was shifted away from Briscoe and onto Heartland. For these reasons, the Petition should be denied.

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[8] Heartland had raised the issue whether the Plan was "fair and equitable" as required under section 1129(b) because Heartland feared the Property would decline in value before it received full payment on its claim. Briscoe explained to the appellate court that "While it is true that the Bankruptcy Court did not make a specific finding regarding the value of the Property fifteen years after confirmation, the Bankruptcy Court had before it credible evidence that the Property would not decline in value." Letter from Marilyn D. Garner to Susan Vaughn, Resp. App. at 3.

III. THE COURT OF APPEALS OPINION REGARDING SEPARATE CLASSIFICATION IS CONSISTENT WITH *GREYSTONE* AND DOES NOT CONFLICT WITH OTHER CIRCUIT COURT DECISIONS

The circuit court decisions are uniform on the issue of separate classification. Each circuit that has addressed the issue has recognized that good reasons may exist to justify separate classification of similar claims. *See In re Greystone III Joint Venture*, 948 F.2d 134 (5th Cir.), *cert. denied*, 113 S. Ct. 72 (1992); *John Hancock Mut. Life Ins. Co. v. Route 37 Business Park Assocs.*, 987 F.2d 154, 161-62 (3d Cir. 1993) (separate classification based on distinction relating to recourse debt differences and proffered business reasons was not justified, but good reasons may exist to justify separate classification); *Lumber Exchange Bldg. Ltd. Partnership v. Mutual Life Ins. Co.*, 968 F.2d 647, 649 (8th Cir. 1992) ("A debtor may classify substantially similar claims separately for reasons independent of the debtor's motivation to secure the vote of an impaired class of claims," citing *Greystone*); *In re Bryson Properties, XVIII*, 961 F.2d 496, 502 (4th Cir.), *cert. denied*, 113 S. Ct. 191 (1992) (separate classification is sustainable if sufficient justification exists, but refusing to sustain separate classification based on "natural" and "unnatural" recourse distinction); *In re U.S. Truck*, 800 F.2d 581, 587 (6th Cir. 1986) (separate classification permitted where the interests of creditors differ substantially; interests other than payment of debt were at stake). Heartland asks this Court to engraft onto the "good reasons" exception a *per se* rule that when similar claims are classified

separately, the plan must treat them differently. No circuit court has adopted this rule, and for good reason.[9]

Heartland presents no cases showing a conflict between the circuits on this issue. Heartland is incorrect insofar as it suggests that there is a conflict between the Court of Appeals Opinion and the Fourth Circuit decision in *Bryson*. Both the Court of Appeals and the *Bryson* court rejected a *per se* rule that would require different treatment of separately classified claims. Furthermore, the Fifth Circuit's denial of the Suggestion for Rehearing *En*

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[9] The proposed rule would not prevent the mischief to be avoided – that of *improper* classification of similar claims to obtain an affirming vote in a cramdown situation. Indeed, the proposed rule itself is subject to manipulation: plan proponents could merely treat separately classified claims differently, whether or not such is necessary, and whether or not there is an improper purpose to gerrymander. Rather than clutter the analysis with a misguided rule, the courts have generally focused on the right question: whether the proposed classification scheme, under the particular facts, constitutes improper manipulation. For example, the Third Circuit requires that the classification scheme be "reasonable" and that "each class must represent a voting interest that is sufficiently distinct and weighty to merit a separate voice in the decision whether a proposed reorganization should proceed." *Route 37 Business Park Assocs.*, 987 F.2d at 159.

Banc dispels any notion that *Greystone* adopted a *per se* rule.[10]

Specifically, in *Bryson*, the Fourth Circuit deemed that according the same treatment to separately classified unsecured claims is "highly suspect." 961 F.2d at 500. Nevertheless, the court explicitly entertained the possibility that the debtor (the plan proponent) could offer reasons for the separate classification that would "withstand scrutiny." *Id.*

Similarly, the Court of Appeals here merely applied the "good reasons" exception in a manner consistent with *Bryson*. That is, the Court of Appeals first acknowledged the general rule of *Greystone* that "thou shalt not classify similar claims differently in order to gerrymander an affirmative vote on a reorganization plan." 994 F.2d at 1167; Pet. App. at 15. Following the Sixth Circuit in *U.S. Truck*, the Court of Appeals explicitly discussed the

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[10] Heartland misreads *Greystone* to require that "good business reasons" are valid only if the different classes receive different treatment under the plan. Pet. at 18. The passage in *Greystone* upon which Heartland relies is dicta and far from an iron clad rule: "Because there is no separate treatment of the trade creditors *in this case*, we reject Greystone's 'realities of business' argument." 948 F.2d at 141 (emphasis added). Moreover, it is clear that the panel below and the Fifth Circuit *en banc* perceived no need to "correct" or even clarify the Panel Opinion, in that both the Petition for Rehearing and the Suggestion for Rehearing *En Banc* were denied.

distinct interest of the City,[11] specifically its non-creditor interests and its contribution of $20,000 a month relating to its urban housing program. 994 F.2d at 1167; Pet. App.

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[11] The City's considerable non-creditor interest in the Property is evident from the following excerpt from closing arguments:

MR. COLVIN: I'll be very brief, Your Honor. Your Honor, the City of Fort Worth through the Trinity Housing Authority has invested in excess of $8 million into this project. This investment was made in order to have built in the city a safe low to moderate income project. We believe that the property and its preservation as a safe low to moderate income property is paramount, at least in the eyes of the City, and for this reason the City voted its unsecured claim in favor of the Plan.

Your Honor, we believe the Plan is feasible. We think the value is as represented by the Debtor.

Your Honor, *this property is a safe harbor in an area of conflict*. And I've only been to the property one time, and that was the time that the Court visited the property. And if there was ever a true statement that a picture is worth a thousand words, a visit to this property was worth many days of testimony.

Your Honor, the City would ask the Court to confirm this Plan. If you consider the down side to Heartland, if the Plan does not work, they get to foreclose. They get exactly what they want. What we're asking for and what the Debtor is asking for is a chance. And this is the court of chance. Give us an opportunity to pay them the true value for this property and to give the citizens of Fort Worth what they bargained for when they invested the money in the project. Thank you.

Confirmation Hearing Transcript, Volume V, at 51-52 (emphasis added).

at 16. The Court of Appeals concluded that the relationship with the City was essential to the continued operation of the housing complex. *Id.* This holding is consistent not only with *Greystone* but also with the case law of other circuits.[12]

Accordingly, there is no conflict in the development of this doctrine in the lower courts; it is appropriate to leave to the lower courts the task of tailoring, on a case-by-case basis, the contours of the justification for separate classification.

Furthermore, even if this Court were inclined to consider the standards for separate classification in typical bankruptcies, the unique fact pattern makes this case a very poor vehicle for that purpose. The multiple roles occupied here by the City would rarely, if ever, reoccur in other cases; thus any ruling by this Court on separate classification of the City's claim in this unusual case

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[12] For example, separate classification of the City's claim allowed Briscoe to maintain an important, ongoing relationship with the City. *See In re LeBlanc*, 622 F.2d 872, 879 (5th Cir. 1980) (special relationship with creditor justified different treatment of similar claims). The City's commitment of $20,000 a month to provide tenant subsidies would arguably have been lost had the City's claim been classified with Heartland's unsecured claim. Other courts have also established that separate classification of similar claims is appropriate where interests other than payment of claims is involved. *In re U.S. Truck Co.*, 800 F.2d 581 (6th Cir. 1986) (separate classification permitted where future interests other than payment of debt were at stake). *In re Atlanta West VI*, 91 B.R. 620, 626 (Bankr. N.D. Ga. 1988) (separate classification of unsecured claim allowed for creditor providing an infusion of new funds under the plan).

would have little value as a guiding precedent.[13] Further, the particular facts in this case establish a separate ground to affirm the lower court's confirmation of Briscoe's Plan under the cramdown provision – a potential quagmire that has nothing to do with the classification issue presented for review.[14] These factual peculiarities would disqualify this case as a candidate for certiorari even if a conflict did exist between the circuits on standards for approving separate classification.

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[13] Indeed, after listing several grounds for concluding that the "city of Fort Worth is distinct from other creditors including Heartland" the Court of Appeals stated, "We emphasize the narrowness of this holding." 994 F.2d at 1167; Pet. App. at 16.

[14] Specifically, the classification issue centers on whether the City's unsecured Class 3 claim was properly classified as separate from Heartland's claim. The record establishes that Class 2 – the City's secured ad valorem tax claim – also voted affirmatively for Briscoe's Plan. Testimony of counsel for the City, Confirmation Hearing Transcript, Vol. III at 83. Even if the City's unsecured Class 3 claim had been improperly classified, the Class 2 vote would arguably qualify as an affirmative vote for the plan such that Briscoe could avail itself of the cramdown provisions. Response of Briscoe to Suggestion for Rehearing *En Banc* at 7-9. The appellate court never discussed this issue, so this Court might need to confront the outcome-determinative question whether the City's affirmative Class 2 vote qualified to trigger the cramdown provisions (which may or may not raise fact questions). Accordingly, after full briefing, the existence of the separate ground to affirm confirmation of Briscoe's plan could result in a decision that certiorari was improvidently granted. *See, e.g., The Monrosa v. Carbon Black, Inc.*, 359 U.S. 180 (1959) (granting of writ was improvident where judgment below was correct on a different ground).

CONCLUSION

None of the issues Heartland presents is worthy of review by this Court. Concerning the burden of proof (Point 1), the Court of Appeals Opinion applies this Court's precedent and does not conflict with any other circuit, but rather accords with a Tenth Circuit decision in this area of the law. With regard to Point 2, the Fifth Circuit did not shift the burden of proof to Heartland on the issue whether the Plan was fair and equitable. Finally, there is no circuit conflict on the classification issue presented by Heartland and the factual predicate for the ruling below on this issue is nonrecurring (Point 3).

For these reasons, this Court should deny Heartland's petition for writ of certiorari.

Respectfully submitted,

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Susan Vaughn, Case Manager
United States Court of Appeals
600 Camp Street
New Orleans, Louisiana 70130

Re: *Heartland Federal Savings and Loan Association v. Briscoe Enterprises, Ltd., II*
Case No. 92-1446

Dear Ms. Vaughn:

Briscoe Enterprises, Ltd., II ("Briscoe") submits the following in response to the Court's March 25, 1993 letter regarding this matter.

A. BURDEN OF PROOF

Briscoe agrees with Professor Warren's conclusion that the appropriate evidentiary burden of proof in a bankruptcy case in general, and in a contested confirmation hearing under section 1129(b) of the Bankruptcy Code in particular, is preponderance of the evidence. Professor Warren suggests that the bankruptcy power is subject to the Fifth Amendment takings clause under "unusual circumstances." That point, however, is the subject of debate. To the extent that the appropriate evidentiary standard depends on the constitutional status of a secured creditor's lien in a bankruptcy case, Briscoe would note to the Court that some commentators question whether the bankruptcy power is subject to the Fifth Amendment at all. *See* Rogers, *The Impairment of Secured Creditors' Rights in Reorganization: A Study of the Relationship Between the Fifth Amendment and the Bankruptcy Clause*, 96 Harv. L. Rev. 973, 1030-31 (1983); Carlson, *Postpetition Interest Under the Bankruptcy Code*, 43 U. Miami L. Rev. (1988). Professor Warren is correct that even if the takings clause is implicated in a bankruptcy case, the appropriate standard is the preponderance standard. To the extent the Fifth Amendment is not implicated, it is clear that preponderance is the proper standard for a contested confirmation hearing under section 1129(b).

This case does not involve any unusual circumstances that would require a stricter burden of proof. Rather, this case involves only a monetary dispute between a debtor and a secured creditor. There is absolutely no rational basis to raise the standard of proof beyond preponderance. Further, the Bankruptcy Code is

silent as to the applicable burden of proof. Because Congress did not include a burden of proof in the statute, the general preponderance of the evidence standard applicable to civil litigation is appropriate in this case. A stricter standard of proof is not warranted.

B. VALUE OF PROPERTY

Professor Warren correctly concluded that balloon payments are permissible, even when the source of funds for payment of the balloon is not determined at confirmation, so long as the bankruptcy court has concluded that the value of the property will not decline. Of course, the confirmed Plan in this case does not provide a balloon in the traditional sense. The principal balance of Heartland's secured claim is amortized during the term of the Plan. Approximately twenty-five percent (25%) of the principal balance of the secured claim will be paid by the end of the fifteenth year. While it is true that the Bankruptcy Court did not make a specific finding regarding the value of the Property fifteen years after confirmation, the Bankruptcy Court had before it credible evidence that the Property would not decline in value. The Bankruptcy Court considered the following factors:

a. Implementation of the Plan requires a minimum income of $200,000 per month. (Briscoe Exhibit 3; Tr. Vol. II, at pp. 87-88);

b. Briscoe had achieved income in excess of $200,000 per month at the end of 1990 and in early 1991, even while the Property was only 85% occupied. (Tr. Vol. II at pp. 83-84);

c. Briscoe will increase the rent on all 784 units by $5 per month beginning July 1991. As a

result, monthly income will increase to $260,000. (Briscoe Exhibits 1 and 2; Tr. Vol. II, at p. 84);

d. Occupancy at the Property is expected to increase substantially. (Tr. Vol. II, at pp. 75-83; Tr. Vol. III at 24);

e. With a minimum income of $200,000 per month, Briscoe can pay its operating expenses, debt service, *ad valorem* taxes and pay for some repairs not covered by the Insurance Proceeds. (Briscoe Exhibits 2 and 6; Tr. Vol. II at pp. 87-96);

f. Repairs (some of which are not immediate) will be made from Insurance Proceeds or net operating income. (Tr. Vol. II, at 104);

g. Turnover rates at the Property range from 25-30% as opposed to a common range of 64-104% in the Dallas/Fort Worth metropolitan area. (Tr. Vol. III, at pp. 21-25);

h. Briscoe has reduced vacancies from approximately 400 to approximately 50 during the case. (Tr. Vol. II at p. 84; at pp. 219-220);

i. The Bankruptcy Court judge visually inspected the Property (Tr. Vol. IV at pp. 156-163) and was impressed with its condition. (Tr. Vol. V at pp. 70-71);

j. Approximately $750,000 in *ad valorem* taxes will be paid prior to the end of the Plan term. (Tr. Vol. II at p. 120);

k. Briscoe will make monthly principal payments to Heartland with interest at the rate of 10.25% per annum. During the term of the Plan, approximately $1.7 million of principal

of Heartland's secured claim will be paid. (Tr. Vol. II, at pp. 121-123). Heartland did not object to the interest rate or the loan term.

l. The City of Fort Worth, throughout the confirmation hearing, supported the continuation of the Property as a safe, clean and affordable low to moderate income residential community. (Tr. Vol. V, at pp. 51-52).

Based on these and other factors, the Bankruptcy Court impliedly found that the value of the Property would remain constant or increase during the term of the Plan.[1] The Bankruptcy Court further found the Plan to be feasible based upon applicable law and this finding is not clearly erroneous. Had the Bankruptcy Court believed that the value of the Property would decline, or that Heartland would not be adequately protected, the Bankruptcy Court could not have found the Plan to be feasible. Consequently, the balloon payment required by the Plan is appropriate.

C. Motivation of the equity interests' efforts in this reorganization considering that its interests are extinguished.

This question can be addressed in two parts. First, Briscoe recognized and discharged its fiduciary duty to its creditors to promulgate a confirmable chapter 11 plan

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[1] *Texas Mortgage Servs. Corp v. Guadalupe Sav. & Loan Assn. (In re Texas Mortgage Servs. Corp.)*, 761 F.2d 1068, 1075 n.12 (5th Cir. 1985) (If a trial judge fails to make a specific finding on a particular fact, the reviewing court may assume that the court impliedly made findings consistent with its general holding).

that would maximize the return to *all* creditors of the estate. Including the undersecured claim of the City of Fort Worth, there are approximately $8 million of creditors (other than Heartland) that have an economic stake in this reorganization. (Tr. Vol. II, at pp. 120-122). The structure of the confirmed chapter 11 Plan allows the maximum recovery to unsecured creditors and ensures that Heartland will receive the present value of its secured claim. Put differently, the creditors, including Heartland, benefit if the Property performs as projected. If the Property fails to perform as projected, however, Heartland will recover its security.

Second, and perhaps most important to Briscoe, Briscoe desires to accomplish a reorganization that will be socially responsible. The Property is not a typical apartment complex. The Property essentially is a 784 unit quasi-public residential community in which the City of Fort Worth invested $7 million for construction. The objective of Briscoe and the City of Fort Worth in constructing the Property was to provide clean, secure, and affordable housing for low to moderate income families residing in an otherwise inhospitable part of Fort Worth, Texas. The Property is located in a high crime and drug traffic area of Fort Worth. Approximately ninety percent (90%) of the residents are African-American, most of whom are single female heads of household. (Tr. Vol. II at pp. 59-62).

The Property offers many desirable amenities that often are not found in low income communities. The Property provides residents with 24-hour security, staffed by at least two security guards at all times, an on-site daycare center, playgrounds, club rooms, swimming

pools, tennis courts, basketball courts, and a video game room. (Tr. Vol. II at p. 61). Crime, while rampant in the surrounding community, is almost non-existent in the Property itself. It is for these and other similar reasons that the City of Fort Worth has supported Briscoe's prior ownership of the Property and the chapter 11 Plan. Neither Briscoe nor the City of Fort Worth have ever been provided any assurance that Heartland would, in the event of a foreclosure, be sensitive to the needs of the residents or maintain the quality and integrity of the Property.

A trust was created under the Plan to ensure the continued viability of the community created by Briscoe and supported by the City. Two of the trustees of the trust created under the Plan will be appointed by the two largest holders of claims represented in the trust – Heartland (holding an approximately $10 million undersecured claim) and the City of Fort Worth (holding an approximate $8 million claim). Because over 90% of the residents of the property are African Americans, and to ensure proper stewardship for the residents and the Property, one trustee will be appointed by the NAACP to represent the community's interests. The mandate of the trust is clear: maintain the quality and integrity of the property for the tenants and surrounding community.

Certainly, the equity owners of Briscoe desired to retain ownership of the Property. Unfortunately, it became clear at the commencement of this bankruptcy case that the equity owners of Briscoe did not have the financial ability to contribute any significant capital to the reorganization effort. Consequently, all thoughts relating to a "new value" plan were quickly replaced with the two

goals discussed above. The equity owners constructed and operated the Property not only to make a profit, but also as a humanitarian and philanthropic endeavor to enhance the lives of others. Consequently, the equity interests remain committed to doing whatever it takes to maintain the Property as a showcase of a premier low-income housing community in the City of Fort Worth.

The purpose of this chapter 11 case was to forge a consensual plan of reorganization. Often, bargains are made under the shadow of the Bankruptcy Code. By creating a "confirmable" chapter 11 plan, the Debtor hoped to foster a negotiated resolution with its most (and only) recalcitrant creditor – Heartland. This strategy, of course, while consistent with the language, spirit, and purposes of the Bankruptcy Code, proved to be unsuccessful in this case. Briscoe looks forward to the Court's ruling in this matter.

Sincerely,

/S/

MARILYN D. GARNER

MDG/ms
cc: Douglas S. Lang
L. Edward Briscoe
Joseph Colvin